Use a TFSA to Maximize Your OAS Benefit

Description

Choosing when to retire can be a worrying, difficult, and life-changing decision for many Canadians. While many wrestle with when to retire, Canadians become eligible for the Old Age Security (OAS) benefit at 65 years of age. The OAS is an important pillar of Canada's aged retirement system, and there are some strict rules regarding eligibility.

Avoiding the OAS clawback

To qualify for a full pension, you must have lived in Canada for 40 years or more since turning 18. The maximum basic monthly payment is $613.53 and increases to $916.38 per month depending on your status. If your annual income equals or exceeds $79,054, then the OAS clawback is triggered**,** reducing the pension by $0.15 for every dollar in excess of the threshold.

There are strategies that can be used to boost retirement income in excess of the threshold while ensuring eligibility for the full basic pension. One of the simplest is to utilize a Tax-Free Savings Account (TFSA) to create the additional income. Aside from the account's tax-sheltered status, which makes all capital gains and dividend payments tax free for the life of the investment, earnings from a TFSA are not counted as taxable income, meaning they don't contribute to the OAS threshold.

Importantly, you can make tax-free withdrawals at any time from your TFSA, the only limitation being the annual cap on contributions. That makes it essential for Canadians to prioritize their TFSA and contribute the maximum allowed each year, using it to buy quality dividend-paying stocks. This will allow them to significantly increase the amount of tax-free income that can be generated, which won't be counted toward the annual limit that triggers the OAS clawback.

The earlier you start contributing to your TFSA, the better, because there will be more time to benefit from compounding investment returns to create a sizable lump sum to generate income in retirement. To accelerate the rate at which you can grow your TFSA balance is to invest in stocks that have a wide economic moat, strong long-term growth, and steadily growing dividends.

An ideal candidate is **Brookfield Infrastructure Partners** (TSX:BIP.UN)(NYSE:BIP), which, after reinvesting distributions, has delivered 857%, or a compound annual growth rate (CAGR) of 25% over the last 10 years. It pays a sustainable distribution, which it has hiked for the last years to be yielding a juicy 3.7%.

Brookfield Infrastructure owns a globally diversified portfolio of infrastructure, including ports, toll roads, utilities, and data centres, which are critical to modern economic activity, meaning that demand for the use of those facilities is relatively inelastic. The partnership possesses a wide, almost insurmountable moat, which, along with operating in oligopolistic markets and generating most of its revenue from contracted or regulated sources, almost guarantees its earnings.

Those characteristics endow it with considerable defensive characteristics, making it resistant to economic downturns. For these reasons, Brookfield Infrastructure is significantly less volatile than many other stocks and the broader market, as illustrated by its beta of 0.80.

When those attributes are combined with Brookfield Infrastructure's strategy of capital recycling, where it sells mature assets and uses the proceeds to make opportunistic acquisition, its earnings will keep growing. That will boost Brookfield Infrastructure's asset value and earnings while supporting the planned 5-9% annual distribution growth.

If you invest your 2020 $6,000 TFSA contribution in Brookfield Infrastructure today, add $6,000 annually, and reinvest all distributions paid, you could accrue around $305,000 in just 10 years. Upon reaching that amount, you could cease reinvesting the distributions and take them as cash, adding around $940 to your monthly income, which is not counted toward the OAS income threshold.

Looking ahead

It is important to note that stocks are a long-term investment, and there is no guarantee that future returns will be the same as past performance. An important tool for managing risk, particularly over the long term and when preparing for such a crucial life event as retirement, is diversification. While Brookfield Infrastructure is a great stock to own in a TFSA, in order to reduce market risk, it is important to invest in other quality companies with similar characteristics across different industries. That includes, but is not restricted to, the Big Six banks, energy infrastructure giant **Enbridge**, and real estate investment trusts.

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